As I See

Volume XXI

MAY 27
1952

Number 21

THE OUTLOOK AT THE PRESENT TIME

NEW building has proceeded faster than anyone thought possible in the first four months of the year, and there is a strong probability that Regulation X will be done away with before the summer is over. There are many people at the present time predicting another million-unit year, but whether we reach the million-unit point or not, it now seems certain that 1952 will be a very good year for general building.

I am relatively optimistic for the remainder of 1952. For the last seven months of the year, inflationary pressures due to the unbalanced budget will be greater than they have been in the first part of the year. Actually, in the first five months the government has had a surplus of receipts over expenses. This is deflationary and is due to the fact that our defense program has bogged down and is not proceeding at the rate originally planned. It seems inevitable, however, that in the next seven months the actual cash disbursements of the government will exceed receipts by at least $5 billion, and this should have a fairly strong stimulating effect on general business during that period.

Another inflationary factor, in my opinion, is that we are apparently going to continue price and wage controls. I have always insisted that controls of this type are inflationary and increase the difficulties which we are trying to correct. Prices rise in a free market when the supply does not equal the demand. The only logical solution is to either reduce the demand or increase the supply. In a free market the price rises in themselves reduce demand and, since they provide a greater incentive to production, increase supply, and the situation is quickly remedied.

In a controlled market an attempt is made to freeze the price somewhere below the point where the controllers think it would otherwise be. If there were only one cost of production, this might work, but in the manufacture of any product there are high-cost producers and low-cost producers, and many falling between the two extremes. In a free market, the price of any product will come into balance with demand when it reaches a point where the highest-cost producer whose production is necessary to satisfy demand can operate with a small profit. On this basis the profit of the low-cost producers is probably substantial, and the profit of the average-cost producer is average.

If the price controllers set the maximum price for any item at a point where the highest-cost producer whose production is necessary to meet the demand could make a profit, there would be no advantage in price control, as the price would not rise above this point were there no price control. If the maximum price is set below the price necessary to furnish a profit to the highest-cost producer whose production is necessary to fill the demand, the high-cost producers are driven from the market and attempt to switch their production to other items on which they can make a profit. This decreases supply at the very time when increased supply is necessary.

It is clearly impossible for the low-cost producers to increase their production to take care of the shrinkage in supply, as they have apparently been trying to maximize their production and their profit all the time. If they could not increase their production when the price was higher, their chance of increasing it by any appreciable amount when the price has been reduced is much less.

Let us look for a minute at the demand side of the picture. Demand is greatly affected by price. As prices go down, the demand for almost all items increases, and as prices rise, the demand for almost all items decreases. Almost anything could be sold in large quantities were the price low enough, and almost any product would lose the greater part of its market were the price to advance by a sufficient amount. Through price control, however, we attempt to solve a shortage in supply by decreasing the supply, and an excess of demand by lowering price, which increases the demand. As a result, a relatively slight excess of demand over supply for any product, which would normally solve itself in a short time, is intensified and perpetuated into a continuing and increased pressure.

The third item which is still highly inflationary in our national set-up is that we still have a managed currency. We left the gold standard in 1933 and we have never returned to it. Our present system, while it retains a few of the characteristics of the old gold standard, at best is nothing more than a "gold-plated" standard.

Money management is not new. There have been many attempts during the past few thousand years by governments to undertake programs for which the citizens were unwilling to pay in taxes, and these projects have accordingly been financed by either attempting to borrow from the future or by creating additional currency and credit. Actually, almost all attempts of government to furnish goods and services in excess of the amount the taxpayers are willing to underwrite in their current tax payments fail, as the excess cost is collected out of a reduction in the purchasing power of all types of savings. Increasing the amount of currency and credit always increases the price level, which means that the purchasing power of all accumulated savings decreases. Whenever we attempt to spend in excess of current tax collections, the purchasing power of the face value of life insurance policies and the purchasing power of savings accounts and time deposits decreases. All bondholders, both government and corporate, lose a portion of their principal through these "hidden taxes."

There has come a day of reckoning in every managed currency the world has ever tried. After inflation reaches a certain point it ceases to be a stimulant and, if it is pushed beyond this point, it produces the peculiar situation of rising commodity prices and stagnating business. This has been quite apparent in many of the inflations in Europe, where German, French and Italian currencies were being inflated, prices were rising rapidly, and the entire area was being reduced to a barter economy which rapidly deteriorated into national bankruptcy and total collapse.

I believe that during 1952 the inflationary pressures listed above, which have been operating now for many years, will gradually be neutralized by other factors, resulting in a sizable readjustment in our entire economy starting some time after this year. It seems to me that the principal neutralizing factors to our inflationary program are:

The inventories in the hands of consumers. We have heard a great deal in the past about manufacturers' inventories and the inventories of retailers, but we have heard relatively little about inventories in the hands of eventual consumers. The war shortages of a few years ago have been filled. We have had a long continuing boom in the sale of all types of durable and semi-durable goods. The older automobiles on the road have been replaced, until the average family has at its disposal transportation facilities which could be used for many years without replacement. While there is still some field for additional television sets, it is quite significant that in the relatively few years in which television has been available, one-third of our families can now watch programs originating in various parts of the United States. We are well equipped with furniture and house furnishings, with electrical appliances and with clothing. The consumer is in a position to defer purchasing on many items if, in his opinion, either the price is too high or the price is likely to drop. The consumer is exercising this prerogative of not purchasing on today's market to a greater extent than he has in the past, resulting in a rather rapid increase in personal savings. This increase during the past year has definitely shown that the consumer prefers not to buy many things under present conditions. This preference for cash is reducing the velocity of turnover of our bank deposits, which in itself is deflationary in its effect on general business.

It seems to me that one of the factors which is generally underestimated in evaluating the future is the effect on many types of business of the rate of new family formation. One of the reasons which I gave for expecting a real estate boom when I wrote The Coming Boom in Real Estate in 1936 was that the marriage rate and birth rate at that time were unusually low but were both increasing. One of my present reasons for caution is that the marriage rate, while still relatively high, is now almost 900,000 marriages per year below the peak, with the very strong probability that it will continue to decrease for the next five years. The very low birth rates of the thirties are responsible for the fact that a smaller percentage of our population is now reaching marriageable age than we would otherwise have, and this drop in the persons reaching marriageable age will

continue at an accelerated rate until approximately 1957. Then, due to the high birth rates of World War II, we will experience a very rapid increase year by year in the number of persons reaching marriageable age, climbing to a tremendous peak between 1965 and 1970. Undoubtedly this period in the sixties will constitute the period of the next big real estate boom in the United States. This next boom should be a boom of tremendous proportions, as the percentage increase in the number of persons reaching marriageable age in those years will be greater than we have ever experienced at any time in our history.

All of our subscribers are familiar with our long cycle charts and with the fact that real estate activity in the United States has followed a rather consistent pattern. Every 16 to 20 years we have had a real estate boom, and these booms have alternated with real estate depressions. Our present real estate boom has now continued for a longer period than any real estate boom we have had in the United States during the past 150 years. Population and family factors would indicate another tremendous boom in the sixties, but these same factors would indicate a reduced rate of real estate activity in the intervening period. How great the dip might be, no one can predict, but it requires more credulity than I possess to believe that a tremendous boom like the one we have just come through can be kept going by additional inflation during a period when the factors which ordinarily cause real estate booms have turned negative.

During the remainder of 1952 every effort will be made to keep the inflationary factors in the ascendancy. Any sizable decrease in employment or in personal income between now and November will be avoided if there is any possible way of avoiding it, and it seems to me that the amount which the government will be pumping out each month in defense expenditures during the rest of 1952 will do the trick. It may be that the day of reckoning may even be postponed during 1953, but the new president of the United States, whoever he might be, will probably find himself in pretty much the position that Herbert Hoover experienced before the end of his term.

Roy Wenzlick

ROY WENZLICK